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Japan's Economy Surges Ahead In Fourth Quarter

Continued strong growth in business investment and a recovery in residential construction led to a sharp expansion in Japan's economy in the October-December period. The increase in gross national product at an inflation-adjusted annual rate of 7.2 percent, compared to 3 percent in the preceding three months (see Table), surprised many economists. Calendar year 1985 growth registered 4.6 percent, a modest slowdown from 1984's 5.1 percent rate.

Private investment increased at double-digit rates for the third consecutive quarter, led by the nonmanufacturing sector. Plant and equipment

outlays by manufacturers slowed, though, reflecting the downward trend in export shipments. Measures to increase home purchases in last October's demand stimulation package (see JEI Report No. 40B, October 18, 1985) encouraged the 9.1 percent rise in residential construction, as housing starts increased each month during 1985's final quarter.

The economy's impressive growth occurred despite the second consecutive quarterly drop in exports. The decline reflected the fall in the yen value of shipments to the United States and China. The external sector, however, made a net positive contribution to growth of about 1 percentage point, as the fall in imports exceeded that of exports.

Personal consumption continued to increase at a sluggish pace, rising just 2.2 percent, because of modest income gains. The increase in income was only 2.8 percent in real terms compared to year-earlier levels. During the past seven quarters, the rise in consumer spending has exceeded 2.2 percent only once.

It is not anticipated that growth in the coming months will match the impressive fourth-quarter results. Most exports for the October-December period were contracted prior to the sharp appreciation of the yen that began in late September. Bigger declines in shipments are expected as the export volume responds to the higher yen. Industrial production was down 3 percent in the last three months of 1985, and the Economic Planning Agency predicts another 0.2 percent fall in the January-March quarter. This would mark the first time production has fallen three consecutive quarters since the 1973 oil crisis. The government plans to announce a package of measures to stimulate domestic demand prior to Prime Minister Yasuhiro Nakasone's departure for Washington on April 12.

The pace of personal consumption expenditures, which accounts for over one-half of GNP, will play a major role in determining whether the current expansion continues. In the six months following the 1978 appreciation of the yen, consumption increased at an inflation-adjusted annual rate of 7.5 percent. Despite a slight drop in the growth of nominal income from fiscal 1977 to fiscal 1978, the fall in the inflation rate from 6.8 percent to 3.4 percent boosted real income and consumer spending.

It is unclear, though, whether the recent appreciation of the yen will lead to an equally sharp dip in the inflation rate. In December the government predicted that the rise in the consumer price index would fall from an already low 2.1 percent in FY 1985 to 1.9 percent in FY 1986. Furthermore, the prospects for wage increases are uncertain. While the unions are pushing for at least a 7 percent hike during the annual spring wage bargaining, the chairman of the Japan Federation of Employers' Associations, Bunpei Ohtsuki, has argued for a 3 percent rise. Forecasters such as Nihon Keizai Shimbun and Nomura Research Institute expect a 4.5 to 4.8 percent increase, which would be less than last year's 5 percent rise.

This year, though, the government has clearly indicated its support for a large wage increase to stimulate domestic demand. The prime minister's Industrial Structure Council recently noted that "both nominal and real wage increases in 1983 and 1984 trailed the rise in productivity," and called for a larger share of national income for wages.

Randall S. Jones

Australia increased steadily as the market for primary commodities, particularly wool, expanded rapidly. But bitter memories lingered in Australia, as may be seen in accounts of the multilateral negotiations leading up to the peace treaty of 1951. Moreover, Canberra maintained strong protection of the domestic manufacturing sector. These factors restricted Japan's share of Australia's overseas purchases to only 2 to 3 percent -- mostly in textile products.

Japan obtained full membership in the General Agreement on Tariffs and Trade in 1955 and continued its campaign for a bilateral trade agreement and most-favored-nation privileges with Australia. In 1957, with much trepidation, government officials in Canberra gave in to pressure and signed an "Agreement on Commerce" with Tokyo. However, the document contained a provision allowing Australia to act unilaterally against Japanese imports thought to be damaging to domestic industry. Australia also withheld MFN status from Japan. Even with these so-called "orderly marketing" aspects, however, the agreement created a storm of protest among Australian manufacturers and greatly disappointed the Japanese.

But the degree of economic complementarity between the two was beginning to be appreciated in Australia, and eventually won out over protectionism. When the 1957 agreement was renegotiated in 1963, the controversial unilateral retaliation provision was dropped and MFN rights were granted to Japan. The volume of goods exchanged was increasing rapidly and the pattern of trade was clearly beginning to change. Australia's textile fiber exports began the start of their slow decline and mineral exports noticeably picked up the slack -- with increased coal and copper ore shipments leading this trend. A decision to lift the embargo on iron ore exports at the start of the decade also boosted mineral exports substantially. Australia's imports from Japan continued to be dominated by textile products, but machinery and motor vehicle sales expanded discernibly -- the beginning of what would become Japan's most significant export category in the next few years.

At the same time, Japan's burgeoning heavy industrial sector consumed large quantities of Australian coal and iron ore. Manufacturing concerns bought more Australian copper ore, bauxite and nonferrous metals. Purchases of beef and food and feed grains also increased enormously. These developments were highlighted when Japan surpassed Great Britain as Australia's largest export market in 1967.

This great expansion in trade was not free from demands for protection from both sides. Japan's beef quotas and Australia's foreign motor vehicle restrictions were prominent examples. However, trade continued to grow throughout the 1970s, notwithstanding the first oil crisis and a deep recession in Australia. Realignments in international economic markets and consequent domestic considerations, however, forced the two countries to begin to look more critically at the pattern of bilateral trade.

As a result of the energy crisis, Japan set about diversifying its sources for agricultural and industrial raw material inputs. Simultaneously, Japan's limited share of Australian manufactured exports and its import restrictions on agricultural goods were raising not a little criticism in Australia.

Tensions came to a head in the mid-1970s when Japan overbought its beef quota and, facing demands from the United States for increased market access, blocked purchases of Australian beef for over a year. Simultaneously, the world sugar market softened and Japan sought a readjustment of prearranged contracts. Both sides charged the other with being unreliable, and similar sentiments showed up in political and diplomatic intercourse. Recognizing the importance of cooperation, in 1976 leaders of the two countries moved to ease strained relations by signing what for Australia was an unprecedented treaty of friendship and cooperation. Nicknamed NARA (Nippon-Australia Relations Agreement), the accord was closely followed by additional agreements concerning fishing rights, science, technology and cultural relations.

Significant amounts of Japanese capital began to flow to Australia during the 1970s despite numerous barriers to foreign investment. Not surprisingly, the largest share of investment went to the mining sector. In this case as well, though, Australian foreign investment policy fluctuated in its degree of receptivity, leading analysts to term attempts by Japan to invest and Australian willingness to accept this investment "countercyclical."

Table 1: Japan's Trade with Australia, 1960-85

(in millions of dollars)

Year	Exports (f.o.b.)	Imports (c.i.f.)	Balance
1960	$144.1	$343.7	$-199.6
1965	313.3	552.1	-238.8
1970	589.0	1,507.7	-918.7
1975	1,739.0	4,156.1	-2,417.2
1980	3,388.9	6,981.6	-3,592.7
1981	4,779.2	7,419.3	-2,640.1
1982	4,580.6	6,961.2	-2,380.6
1983	4,280.0	6,641.5	-2,361.7
1984	5,184.3	7,296.4	-2,112.2
1985	5,379.0	7,452.2	-2,073.2

Source: Japan Tariff Association, The Summary Report: Trade of Japan

Recent Trends in Australia's Economy

In the last several years relations between Australia and Japan have been affected by significant domestic economic developments. (For Japanese coverage see JEI Reports No. 3A, January 24, 1986, and 8A, February 28, 1986). Developments in Australia, which not too ironically parallel those in Japan, include the commitment by Prime Minister Robert Hawke's Labor government to liberalize financial markets and ease trade barriers, and the refreshingly amiable pay accord worked out between the government and the usually militant labor unions. Australia's domestic economic recovery since the beginning of the decade has occurred at the same time that the Australian dollar has been

allowed to float, interest rates have soared, contributing to an already well-marked tendency to import capital, and the nation's overall current account deficit has widened.

The current state of Australia's overall trade is important to note. During the first half of 1985 the country ran a trade surplus. But buoyant domestic demand unsatisfied by Australian-made goods boosted imports and reversed this condition in the second half of the year. Despite a prolonged plunge in the value of the Australian dollar against both the yen and the U.S. dollar, demand for imports has remained strong. Moreover, a depreciating currency has not aided Australian efforts to boost exports. The fall in international oil prices and weaker worldwide commodity prices have conspired to prevent the rise in shipments needed to trim the trade deficit. Australia runs a narrowing surplus with Japan, in part because orders from steel mills for iron ore and coal have lagged with the economic slowdown there and elsewhere in the world, compounding the difficulties.

(a) The TWI has been rebased to the March quarter 1981 = 100 and therefore differs from the figures shown in the table.
(b) Upward (downward) movements represent appreciation (depreciation) of the $A against other currencies.
(c) Monthly rates calculated as average of daily rates.

Source: Australia, Department of the Treasury, The Round-up, January 1986

The sustained drop in the value of the Australian dollar since February 1985 has renewed inflation and eroded confidence in the economy. The bad numbers have been a boon to the Hawke government's political opposition and a rallying cry for the hard-hit manufacturing sector. The Australian dollar has dropped to an unprecedented low of less than 70 cents to the U.S. dollar -- a psychological, if not actual, breach of Australian perceptions. (A more important indication comes from the currency's 25 percent drop in 1985 against a trade-weighted basket of currencies.) Last month Brian Powell of the

Australian Chamber of Commerce called on Australia to "wake up and wake up fast" to the trade deficit, inflation and the growing foreign debt. Observers have pointed out that Australia has fallen from being the eighth-largest exporter in the world to 23rd place.

Mr. Hawke and his finance department officials have thus been put in the position of defending their policy and tirelessly explaining the "J-curve effect." Australian Treasury representatives modestly estimate that the currency depreciation will eventually bring down the trade deficit from 4.9 percent of gross domestic product to 4.6 percent, with imports falling by 2 percent and exports rising by around 4.5 percent.

To actually get to this point, the Australian government is pinning its hopes on an improved performance by the manufacturing sector, increased trade in services and a rise in tourism. The carefully worked-out accord with labor was arranged for this purpose as well as to control inflationary pressures linked to wages that were previously adjusted every six months. The government hopes that enhanced confidence in the stability and reliability of Australian producers will stimulate exports of manufactured goods and spur employment opportunities. It also hopes to rekindle the interest of foreigners anxious to invest abroad. the Hawke government has made good on its promise to deregulate and internationalize the Australian banking system and loosen some foreign investment controls. This development is covered below.

Bilateral Trade

Japan's Imports from Australia - During the past five years Australia has continued to supply the raw materials needed by Japan. But the continuing shift of the Japanese economy from heavy manufacturing like steel to high technology industries has curbed demand. Furthermore, Japan's attempts to diversify resource suppliers and a slowing of economic growth have begun to substantially realign its previous trade patterns.

Japan's major imports from Australia include coal, iron ore, nonferrous metal scrap, aluminum, wool, cotton, beef, wheat, sugar and recently oil. Australia's share of total Japanese imports, which reached a peak of 9.4 percent in 1972, has declined to 5 percent-plus since 1980. In 1985 Australia ranked fifth as a supplier of goods to Japan (behind the United States, Saudi Arabia, Indonesia and the United Arab Emirates). Nonetheless, Australia's importance in Japanese markets is enhanced by the fact that it supplies half of all Japan's coal and iron ore as well as almost two-thirds of its beef and wool.

Due to Australia's key role as a supplier of industrial and agricultural inputs, Japan consistently runs a deficit in bilateral trade, although the flood of red ink has ebbed somewhat in recent years, in large part because purchases were no higher in 1985 than in 1980. This situation can be explained several ways. There are analysts who insist that Australia's price competitiveness has deteriorated, and that its suppliers seem to have difficulties meeting the demands of Japanese buyers. It is also noted that Japan has diversified its sources of supply for price, security and political reasons, and this has had an adverse impact on purchases from Australia. There are also those in Australia who claim, as do many in other countries, that Japan has raised barriers to imports that are very difficult to overcome.

All these suggestions have some merit, but the narrowing deficit can also be attributed to the drop in Australia's traditional raw material exports. Reduced requirements for coal, metal ores and textile fibers, which accounted for some 25 percent of Japan's overall imports in 1970, cut the share of these three categories to just 10 percent of the total in 1985. Consequently, Australia's penetration of Japanese markets has dropped overall, with dramatic declines in its share of Japan's food and fiber imports, and less marked but significant declines in ores.

In individual commodity terms, however, the trend seems less clear. Australia's share of Japanese markets for bauxite, beef and wool has indeed deteriorated, while sales of sugar have declined in volume along with those of other major suppliers. But its share of Japanese purchases of iron ore and wheat has held steady, and Australia as well as China and South Africa have increased their shares of the market for coal. It is perhaps most correct to conclude, at this point, that although several of Australia's traditional exports to Japan have suffered recently, some Australian goods have benefited from changes in the structure of Japan's economy.

Table 2: Japan's Imports from Australia, 1981-85

(in millions of dollars, c.i.f. value)

	1981	1982	1983	1984	1985
Total	$7,419.3	$6,961.2	$6,641.5	$7,296.4	$7,452.2
Food Products	1,396.8	1,164.2	1,031.4	1,209.0	1,119.8
Meat	405.6	390.6	389.0	364.1	343.1
Fish	174.2	172.5	162.1	159.7	181.0
Wheat	192.2	184.7	181.8	186.0	172.6
Sorghum	67.6	51.4	14.2	140.2	96.8
Sugar	267.4	114.9	104.2	81.6	61.0
Textile Materials	621.2	612.8	448.6	549.2	545.8
Wool	518.5	481.8	370.0	436.0	429.0
Cotton	100.0	126.3	75.2	109.4	114.0
Metal Ores and Scrap	1,817.5	1,905.7	1,741.5	1,815.8	1,693.6
Iron Ore	1,377.8	1,476.3	1,322.7	1,356.0	1,228.2
Nonferrous Metal Scrap	334.2	354.2	346.3	386.9	382.7
Metals	223.7	245.1	270.0	471.5	453.3
Nonferrous Metals	212.3	218.3	230.9	444.3	442.2
Mineral Fuels	2,674.9	2,516.5	2,648.0	2,690.8	2,960.1
Coal	2,287.9	2,164.5	2,223.2	2,332.9	2,254.6
Crude Oil	16.8	3.3	18.5	37.4	345.5
Other Agricultural and Industrial Inputs	166.8	160.0	160.3	180.3	174.4
Nonmetallic Mineral Ores	104.6	97.0	100.9	109.1	110.0
Chemicals	204.0	86.0	57.9	64.3	44.5
Machinery and Transport Equipment	14.5	17.3	28.2	37.5	59.2
Other	300.1	253.5	255.7	278.0	401.7

Source: Japan Tariff Association, The Summary Report: Trade of Japan

Nevertheless, due largely to past incidents, Australia is extremely sensitive to the overall drop in its penetration of Japanese import markets. Its apprehensions are centered on the implications of continuing Japanese market opening plans. Specifically, there is fear that concessions to the United States and Europe, particularly concerning agricultural products, will cost Australia market share. A highly politicized topic in this regard concerns beef exports. When Tokyo accommodated U.S. requests in April 1984 to up purchases of high-quality (grain fed) beef after years of difficult bilateral negotiations, Australian market opportunities were in effect cut. Japan later promised to raise aggregate beef imports from 135,000 metric tons in FY 1982 to 177,000 metric tons in FY 1987, but Canberra continues to seek assurances that it will not be forgotten among Japan's other trading problem priorities.

Japan's Exports to Australia - Japan's deliveries to Australia are hardly striking in terms of total Japanese exports; they have not exceeded 4 percent in the last thirty years. However, Japan is a very important supplier for Australia. After a temporary dip in market share during the late 1970s, Japan's exports to Australia began to expand and by FY 1983 (July 1983-June 1984) Japan had outstripped the United States as the largest supplier of Australian imports. During that year Japan was the source of 22 percent of Australia's total imports, and the trend shows no sign of slowing.

This state of affairs creates numerous political sensitivities. In a manner all too similar to the ongoing debate in the United States, Australians are asking themselves about structural change in their economy and its implications for manufacturing, especially new industries. Alarm is registered by the quickly eroding trade surplus as Japanese exports grow at a faster rate than its purchases from Australia. Many in Canberra realize all too well that the country is increasingly dependent on Japanese products, while the Japanese are anything but dependent on Australian export markets. Those with a more long-term perspective warn that Australia may end up locked into a dependent relationship arising from a reliance on Japanese-made high technology products.

Without discounting factors such as consumer tastes and spending patterns, an important reason for the degree of Japanese market penetration is price competitiveness. Australian labor costs and price performance have been steadily deteriorating relative to those of Japan since 1970, according to Australian government estimates.

Japan's most important export is motor vehicles. Despite restrictions designed to protect domestic automotive manufacturers, exports of motor vehicles from Japan have grown to represent one-fourth of that country's total shipments to Australia. This is particularly evident in the car market; Japanese vehicles account for two-thirds of all imported cars and around 15 percent of the total Australian market. These percentages will undoubtedly grow larger. In a significant policy turnaround consistent with liberalization goals, the Australian government has initiated a "Car Industry Plan" that will remove tariff and quota prohibitions on auto imports and restrictions on partially manufactured motor vehicles by 1992. This is a market opening move that Canberra hopes will pay off with more Japanese confidence in the Australian marketplace and enhanced investment.

Table 3: Japan's Exports to Australia, 1981-85

(in millions of dollars, f.o.b. value)

	1981	1982	1983	1984	1985
Total Exports	$4,779.2	$4,580.6	$4,280.0	$5,184.3	$5,379.0
Food Products	30.8	26.7	27.7	33.5	27.4
Textiles and Apparel	232.3	232.0	243.0	259.0	224.7
Synthetic Yarn	39.1	37.8	42.2	42.4	35.0
Cotton Fabrics	43.8	50.9	51.9	63.1	47.8
Synthetic Fabrics	66.8	78.2	88.0	84.3	76.1
Chemicals	253.5	198.7	198.1	221.6	214.0
Plastic Materials	74.5	56.9	58.9	76.9	71.8
Manufactured Nonmetallic Mineral Products	90.2	70.5	57.7	76.2	79.9
Metals and Metal Products	499.2	561.5	283.8	360.0	308.2
Steel	375.2	381.7	199.3	236.1	206.0
Metal Products	96.8	160.1	75.8	109.8	90.9
Machinery and Transport Equipment	3,255.9	3,132.7	3,107.1	3,815.8	4,107.5
Power Generating Machinery	117.3	118.8	103.4	108.1	118.4
Office Machinery	129.7	142.4	192.2	251.9	316.2
Metalworking Machinery	72.3	61.6	21.4	55.2	77.1
Electric Power Machinery	73.2	97.2	72.6	54.6	65.7
Television Sets	76.8	48.8	44.7	51.9	47.1
Radio Receivers	67.2	66.2	52.9	74.4	82.1
Motor Vehicles	1,008.2	1,020.7	1,000.9	1,295.1	1,362.7
Motorcycles	105.4	75.5	73.3	71.4	66.0
Ships	159.9	93.6	79.2	36.9	55.3
Scientific and Optical Equipment	135.0	108.2	113.5	140.8	164.2
Audio and Video Recorders	148.1	190.5	280.6	259.1	191.9
Other	417.3	358.3	362.6	418.3	417.2
Tires and Tubes	89.8	80.3	65.6	97.3	86.2

Source: Japan Tariff Association, The Summary Report: Trade of Japan

Japanese manufacturers of nonelectric and electric machinery, chemicals and scientific instruments have made major inroads in the Australian market; in fact, Japan's share of the electric machinery import category stands at about one-third. On the other hand, declining Japanese price competitiveness in industries such as steel has reduced its share of those Australian import markets.

It is also worth noting that Japanese firms are successfully competing for large infrastructure projects. These undertakings are often financed by a consortium of Australian and Japanese public and private sources. A notable example is the newly announced 1.5-mile undersea tunnel linking the port of

Sydney with a northern suburb, which will begin in 1987. Japanese construction firms are also heavily involved in hotel construction and other building projects -- a development that has not gone without notice and expressions of concern from some Australians.

Investment Flows

Although it is conceivable that Australian investors may someday play a role in Japanese financial markets, the extent of that involvement today is negligible. According to Australian data for the early 1980s, Japan amounted to only about 5 percent of Australia's equity investment abroad. As part of Tokyo's recent financial market liberalization moves, four major Australian banks have gained permission to start full retail banking operations in Japan. Australia has also recognized the new opportunities for borrowing, and the benefits of increased access to the Tokyo stock exchange. But these developments are still only in the realm of possibility.

Table 4: Japan's Direct Investments in Australia, FY 180-FY 1984

(in millions of dollars)

FY 1980	$431
FY 1981	348
FY 1982	370
FY 1983	166
FY 1984	105
Cumulative Investment March 31, 1985	3,153
Share of Total Japanese Direct Foreign Investment	4.4%

Source: Ministry of Finance

The opposite is true of activity in the other direction. Based on developments over the last three years, Japanese capital flows to Australia show a great potential for growth. In the July 1984-June 1985 period, Canberra's data indicate, Japan squeezed out the United States and the United Kingdom as Australia's largest source of direct and portfolio investment.

The overall increase in Japan's investment in Australia is due to three factors: the liberalization of Australian (and Japanese) capital markets; the global rise of Japanese capital outflows, which began in 1981; and the gradual rise in foreign borrowing by the Australian government and private corporations.

Another major feature of Japanese investment in Australia is the radical change in its composition. Ten years ago direct investment represented over 80 percent of the total. By the start of the mid-1980s, in contrast, almost

two-thirds of total Japanese investment consisted of portfolio investment and institutional loans.

This shift obviously corresponds to the increased borrowing activity of the Australian government. In the 1960s and 1970s import-restrictive policies were designed not only to protect domestic industry but also to keep foreign debt low. As the Australian dollar came under pressure and the balance of payments suffered, this policy was reversed. Debt rather than equity became the rule in foreign capital transactions.

Foreign investment is the subject of some debate in Australian politics. In fact, although certain controls have been relaxed, Mr. Hawke's government has moved more cautiously in liberalizing foreign investment than many business interests would like. Recently, for example, the Australian government decided to retain the Foreign Investment Review Board, which monitors foreign equity investment, although it did ease some of the terms for review.

Some 43 percent of Japan's investment in Australia between 1951 and 1983 went into primary industries; in contrast, only around 20 percent of all foreign investment in Australia over this period was earmarked for this sector. A sectoral breakdown based on Australian estimates further reveals that Japanese investment in Australian manufacturing accounted for 25 percent of its total (as opposed to 33 percent for all foreign investors), while services absorbed 32 percent (47 percent overall).

Recent figures show a new orientation. Japanese investment in the finance, insurance, real estate and service sectors rose from around 12 percent of the annual total during the Australian FY 1978-FY 1980 period to about 57 percent annually during the FY 1981-FY 1983 period. In contrast, investment in manufacturing skidded from 48 percent of yearly equity investment to just 2 percent. At the same time, Japanese direct investors continue to channel a large -- and growing -- proportion of their investments into mining despite doubts about the stability and competitiveness of this sector of the Australian economy. The share of total Japanese investment going into mining averaged close to 60 percent in three of the four years between FY 1980 and FY 1983.

The concentration of Japanese direct investment in the mining industry is a natural outcome of Japan's reliance on stable foreign supplies of industrial raw materials. In the past year, however, the flow of money to the mining sector fell as relatively few new development projects were floated. Prospects are looking up a bit for this year, though, since the Australian government agreed in early March to allow a consortium in which the Japan National Oil Corp. has a 50 percent stake to engage in oil exploration off the north coast of Australia.

Japan's involvement in the Australian financial sector is clearly linked to the liberalization of financial markets and the deregulation of the banking industry in both countries. In February 1985 Australia invited 16 overseas banks to establish full banking operations. Three Japanese banks were included -- the Bank of Tokyo, Ltd., Mitsubishi Bank, Ltd. and the Industrial Bank of Japan, Ltd. Although some critics oppose Australia's decision, the government anticipates that foreign investment will increase the efficiency of the banking sector, facilitate two-way trade and allow Australia to establish itself abroad by negotiating reciprocal banking rights.

It is expected that within the next five years the 16 new banks will command 20 percent of Australia's banking business. This may be assumed to be mostly due to activities like investment banking and foreign exchange operations rather than to retail and wholesale services. The Japanese banks seem to be moving cautiously, but there is some indication of their interests. They reportedly plan to establish only 15 retail branches between them, compared with as many as 130 branches envisioned by the five new U.S. banks.

Conclusion

Despite ongoing feelings of anxiety on both sides, it seems clear that economic relations between Australia and Japan will continue to flourish, for the essential complementary nature of their two nations remains intact. This optimism is justified by the generally constructive tone of discussions about the relationship by policymakers and industry representatives.

Clearly some degree of tolerance and education has been engendered by past altercations. Australian policymakers often remind the public and themselves that the country's relationship with Japan is really only one side of Japan's larger triangular relationship with the rest of the developed world, and Australia can only demand a reasonable amount of attention. At the same time, there is close interest in the opportunities effected by Japan's market liberalization moves, and a determination to seek out ways to deepen the economic ties between the two countries. Japanese officials respond sensitively to Canberra's feeling of vulnerability and applaud efforts to liberalize the Australian economy that in so many ways parallel Tokyo's own.

Indeed, if there is any one observation to make about the state of relations between the two countries, it is that the tremendous pace of change has not upset affairs between them. Change has, in fact, brought more discussion and examination of the dynamics of the relationship and challenged policymakers in both countries to broaden the context of their thinking about economic planning.

For further information, contact Sheri Hoptman.

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The views expressed in this report are those of the author and do not necessarily reflect those of the Japan Economic Institute.